

AR37

Prairie Oil Royalties

COMPANY, LTD.



ANNUAL REPORT

1977

Directors:

Donald D. Barkwell Calgary, Alberta
*Vice-President, Natural Resources
Norcen Energy Resources Limited*

Edward A. Galvin Calgary, Alberta
*Vice-Chairman of the Board
Norcen Energy Resources Limited*

Wilfrid A. Loucks Calgary, Alberta
*President
Coleman Collieries Limited*

Frederick A. McKinnon Calgary, Alberta
Retired

Clifford A. Rae Calgary, Alberta
*Barrister & Solicitor
Macleod Dixon,
Barristers & Solicitors*

David M. Tyerman, Q.C. Regina, Saskatchewan
*Barrister & Solicitor
MacPherson, Leslie & Tyerman
Barristers & Solicitors*

Officers:

Donald D. Barkwell *President*
*Vice-President, Natural Resources
Norcen Energy Resources Limited*

Richard S. Buckland *Vice-President, Exploration*
*General Manager, Canadian Exploration
Norcen Energy Resources Limited*

Arthur L. Wood *Vice-President, Production*
*General Manager, Oil and Gas production
Norcen Energy Resources Limited*

David M. Tyerman, Q.C. *Secretary*
*Barrister & Solicitor
MacPherson, Leslie & Tyerman
Barristers & Solicitors*

A. Kenneth Davies *Treasurer*
*Treasurer
Norcen Energy Resources Limited*

William T. Kilbourne *Assistant Secretary*
*Vice-President, Legal and Secretary
Norcen Energy Resources Limited*

Russell G. Rennie *Assistant Secretary*
*Assistant Secretary
Norcen Energy Resources Limited*

DESCRIPTION OF BUSINESS

Prairie Oil Royalties Company, Ltd. was incorporated July 13, 1951 under the laws of the Province of Saskatchewan, Canada. The Company produces and sells crude oil, gas liquids and natural gas in Western Canada and is engaged in oil and gas exploration and development in Western Canada and the Canadian Arctic.

ANNUAL GENERAL MEETING

The Annual General Meeting of the Company will be held on Friday, April 28, 1978 at 10:30 o'clock in the forenoon, local time, in the Board Room of Norcen Energy Resources Limited, 32nd Floor, 715 - 5th Avenue S.W., Calgary, Alberta, Canada T2P 2X7.

Executive Office:

715 - 5th Avenue S.W., Calgary, Alberta T2P 2X7

Registered Office:

2161 Scarth Street, Regina, Saskatchewan S4P 2V4

Auditors:

Thorne Riddell & Co., Calgary, Alberta

Registrars & Transfer Agents:

Canada Permanent Trust Company,
Regina, Saskatchewan, and Toronto, Ontario

Morgan Guaranty Trust Company of New York,
New York, N.Y.

Stock Exchange Listings:

Toronto Stock Exchange, Toronto, Ontario
American Stock Exchange, New York, N.Y.

Directors' Report to the Shareholders

FINANCIAL

Revenue, cash flow and earnings reached record high levels in 1977. Revenue totalled \$3,441,000, an increase of \$945,000 or 38 per cent over 1976 revenue. This increase is the result of higher oil and natural gas production and prices and higher interest income. Cash flow was \$2,700,000 or \$1.38 per share compared to \$2,013,000 or \$1.03 per share in 1976. Net earnings were \$1,752,000 or \$0.89 per share compared to net earnings before extraordinary item in the same period last year of \$1,246,000 or \$0.63 per share. Net earnings for the same period in 1976 including extraordinary item were \$5,540,000 or \$2.82 per share.

PRODUCTION

Average daily production for 1977 before deducting royalties was 562 barrels of oil and gas liquids and 5,792 Mcf of gas, compared to 507 barrels and 5,295 Mcf in 1976. The increase in oil and gas liquids production reflects further increases in production levels in Saskatchewan where the Company has substantial royalty interests. The increase in natural gas production results from the installation of new facilities in the Big Bend area and the commencement of production from the Verger area.

The price of western Canadian crude oil increased \$1.00 per barrel on July 1, 1977 and January 1, 1978. The average price received by the Company for crude oil production in 1977 was \$8.96 per barrel compared to \$7.86 in 1976. Increases in the price of natural gas during 1977 raised the Company's average price to \$1.28 per Mcf from an average of \$1.01 per Mcf in 1976.

DRILLING

During the year the Company participated in the drilling of 51 (13.44 net) wells which resulted in 3 oil (.92 net) wells and 34 gas (8.75 net) wells. This activity is summarized in the following chart.

Wells Drilled	1977		1976	
	Gross	Net	Gross	Net
Exploratory				
Oil	2	.42	1	.04
Gas	5	1.17	5	1.06
Dry	13	3.21	17	3.38
	<u>20</u>	<u>4.80</u>	<u>23</u>	<u>4.48</u>
Development				
Oil	1	.50	3	.47
Gas	29	7.58	22	5.12
Dry	1	.56	4	1.05
	<u>31</u>	<u>8.64</u>	<u>29</u>	<u>6.64</u>

DEVELOPMENT

A new sulphur removal plant went into service in the Big Bend area in November, 1977. These facilities, together with new compression facilities placed in operation in April, 1977 are expected to bring the Company's share of production to approximately 4,000 Mcf per day during 1978.

A major expansion of the Verger shallow gas project is nearing completion. A total of 28 wells in which the Company has an interest were drilled and completed in the latter part of 1977 and early 1978 and a further two wells will be drilled during the year. The pipeline gathering system has been installed and daily production for the project has been increased to a rate of 12,600 Mcf from a previous low in January, 1978 of 5,900 Mcf. It is anticipated that the project will be capable of peak production of 14,000 Mcf (Company's share 2,000 Mcf per day) when all new wells are tied in but actual production will depend upon the level of demand by the pipeline company during the coming months.

A four well drilling program is proceeding in the Cherhill area where one well has been drilled and completed recently. Two more locations are awaiting the availability of a drilling rig. The Company has a 50% interest in this lease.

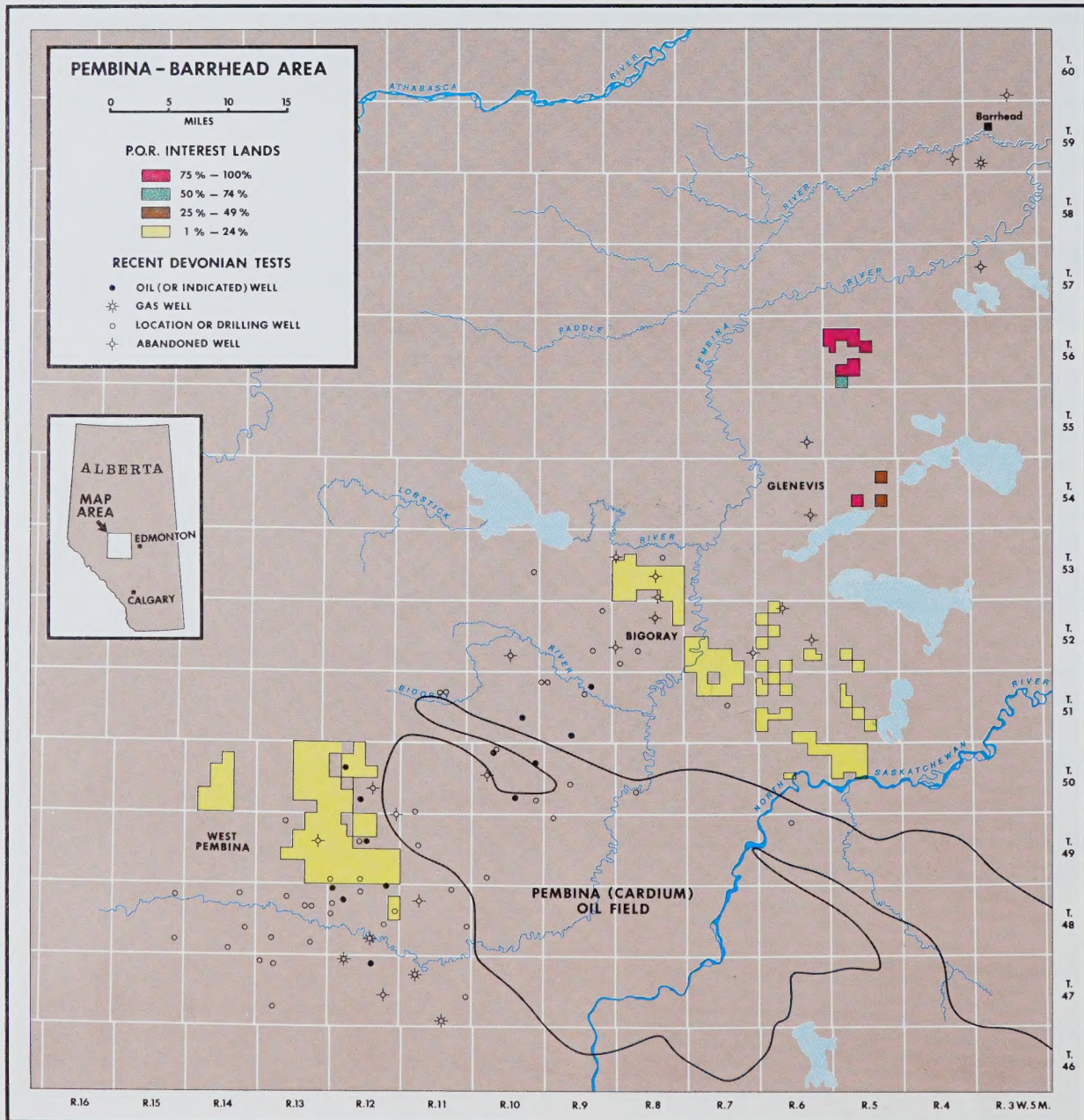
EXPLORATION

The Company concentrated its exploratory activity during 1977 in the Province of Alberta and in particular in the Big Bend gas area north of Edmonton, and in the Pembina-Glenevis area of West Central Alberta. This latter area is shown on the accompanying map.

Considerable interest has developed in the Pembina-Glenevis area during the past year as a result of oil discoveries in the Devonian (Nisku) formation at a depth several

thousand feet below the Cardium formation which has produced oil for the past 24 years. These discoveries have resulted in large expenditures for exploratory acreage and intensive geophysical and drilling activity by the industry including the Company.

The Pembina-Glenevis map in this report shows the land holdings in which the Company has interests. These holdings total 119,508 gross acres equivalent to 15,936 net acres.



To date one oil well has been completed and two wells abandoned on the Company's Pembina-Glenevis lands. However, detailed results of activities during 1977 and 1978 have not been released. Information from the wells drilled will assist in the planning of active seismic and drilling programs during the remainder of 1978.

The potential of this area is by no means established at this time.

OIL AND GAS LANDHOLDINGS

At December 31, 1977, the Company owned interests in 3,339,042 gross (345,244 net) acres compared to 3,543,094 gross (363,738 net) acres at the end of the prior year. These landholdings are shown in detail in the summary at the foot of this page.

GENERAL

Although the decision of the Supreme Court of Canada late in the year regarding the CIGOL (now Norcen Energy Resources Limited) litigation with the Government of Saskatchewan confirmed that company's

position regarding federal/provincial rights under the British North America Act, the Saskatchewan government has passed new legislation retroactive to January 1, 1974. This new legislation could offset the effect of the Supreme Court decision in the matter of the recovery of certain taxes and royalties paid to that government by companies such as Prairie Oil Royalties Company, Ltd. Norcen has reserved the right to pursue this matter further depending on the exact nature and content of the new legislation.

On Behalf of the Board



D. D. Barkwell
President

Calgary, Alberta
April 3, 1978

OIL AND GAS LANDHOLDINGS

	Leases		Reservations, Permits & Licences		Total	
	Gross Acres	Net Acres	Gross Acres	Net Acres	Gross Acres	Net Acres
Arctic Islands	102,493	3,227	2,029,464	81,935	2,131,957	85,162
Banks Island NWT	—	—	183,656	5,785	183,656	5,785
Alberta	546,965	151,062	293,208	42,104	840,173	193,166
British Columbia	519	207	—	—	519	207
Manitoba	72,642	20,928	—	—	72,642	20,928
Saskatchewan	63,215	35,308	46,880	4,688	110,095	39,996
	<u>785,834</u>	<u>210,732</u>	<u>2,553,208</u>	<u>134,512</u>	<u>3,339,042</u>	<u>345,244</u>

In addition to the above, royalty interests are held in 256,422 acres and net carried interests in 1,920 acres.

CONSOLIDATED STATEMENT OF EARNINGS

years ended December 31, 1977 and 1976

	<u>1977</u>	<u>1976</u>
REVENUE		
Oil and gas sales	\$ 1,748,294	\$ 1,362,415
Royalties	982,806	687,910
Interest	710,169	446,262
	<u>3,441,269</u>	<u>2,496,587</u>
EXPENSES		
Production	321,517	201,576
General and administrative	188,107	134,759
Depletion	364,387	293,841
Depreciation	74,551	38,970
	<u>948,562</u>	<u>669,146</u>
Earnings before income taxes and extraordinary item	<u>2,492,707</u>	<u>1,827,441</u>
INCOME TAXES		
Current	231,867	147,489
Deferred	509,000	433,800
	<u>740,867</u>	<u>581,289</u>
Earnings before extraordinary item	<u>1,751,840</u>	<u>1,246,152</u>
EXTRAORDINARY ITEM		
Gain on sale of investment in British Columbia Oil Lands Ltd. (net of applicable income taxes of \$368,000)	<u>—</u>	<u>4,293,502</u>
NET EARNINGS	<u>\$ 1,751,840</u>	<u>\$ 5,539,654</u>
PER SHARE		
Earnings before extraordinary item	\$0.89	\$0.63
Extraordinary item	<u>—</u>	<u>2.19</u>
Net earnings	<u>\$0.89</u>	<u>\$2.82</u>

CONSOLIDATED STATEMENT OF RETAINED EARNINGS

years ended December 31, 1977 and 1976

	<u>1977</u>	<u>1976</u>
BALANCE AT BEGINNING OF YEAR	\$11,046,307	\$ 5,506,653
Net earnings	1,751,840	5,539,654
BALANCE AT END OF YEAR	<u>\$12,798,147</u>	<u>\$11,046,307</u>

BALANCE SHEET

as at December 31, 1977 and 1976

Assets

CURRENT ASSETS

	1977	1976 (consolidated — note 1)
Cash and short-term deposits	\$ 8,524,680	\$ 9,523,428
Accounts receivable	681,484	620,400
Income taxes recoverable	97,033	—
Drilling and other deposits	52,449	47,193
	<u>9,355,646</u>	<u>10,191,021</u>

PROPERTY, PLANT AND EQUIPMENT,

At cost (note 2)	13,679,174	10,519,790
Accumulated depletion and depreciation	3,599,886	3,160,948
	<u>10,079,288</u>	<u>7,358,842</u>
	<u>\$19,434,934</u>	<u>\$17,549,863</u>

Liabilities

CURRENT LIABILITIES

Accounts payable	\$ 753,933	\$ 784,542
Due to parent company	179,204	15,050
Income taxes	—	509,314
	<u>933,137</u>	<u>1,308,906</u>

DEFERRED INCOME TAXES

	<u>3,167,800</u>	<u>2,658,800</u>
--	------------------	------------------

Shareholders' Equity

CAPITAL STOCK

Authorized		
2,500,000 shares of \$1 par value		
Issued		
1,961,520 shares	1,961,520	1,961,520

CONTRIBUTED SURPLUS	574,330	574,330
---------------------------	---------	---------

RETAINED EARNINGS (note 3)	12,798,147	11,046,307
----------------------------------	------------	------------

	<u>15,333,997</u>	<u>13,582,157</u>
--	-------------------	-------------------

Approved by the Board:

	<u>\$19,434,934</u>	<u>\$17,549,863</u>
--	---------------------	---------------------

D. D. Barkwell, Director

W. A. Loucks, Director

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

years ended December 31, 1977 and 1976

	1977	1976
SOURCE OF FUNDS		
Operations		
Earnings before extraordinary items	\$ 1,751,840	\$ 1,246,152
Charges not requiring funds	947,938	766,611
Funds generated from operations	2,699,778	2,012,763
Proceeds from sale of investment in		
British Columbia Oil Lands Ltd.	—	6,302,620
	2,699,778	8,315,383
APPLICATION OF FUNDS		
Property, plant and equipment	3,159,384	1,759,141
INCREASE (DECREASE) IN WORKING CAPITAL	<u>\$ (459,606)</u>	<u>\$ 6,556,242</u>
SUMMARY OF CHANGES IN WORKING CAPITAL		
Increase (Decrease) in current assets		
Cash and short-term deposits	\$ (998,748)	\$ 7,287,071
Accounts receivable	61,084	277,343
Income taxes recoverable	97,033	(50,000)
Drilling and other deposits	5,256	(30,296)
	<u>(835,375)</u>	<u>7,484,118</u>
Decrease (Increase) in current liabilities		
Accounts payable	30,609	(403,512)
Due to parent company	(164,154)	(15,050)
Income taxes	509,314	(509,314)
	<u>375,769</u>	<u>(927,876)</u>
Increase (decrease) in working capital	<u><u>\$ (459,606)</u></u>	<u><u>\$ 6,556,242</u></u>

Auditors' Report

TO THE SHAREHOLDERS OF
PRAIRIE OIL ROYALTIES COMPANY, LTD.

We have examined the balance sheet of Prairie Oil Royalties Company, Ltd. as at December 31, 1977 and 1976 and the consolidated statements of earnings, retained earnings and changes in financial position for the years then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1977 and 1976 and the results of its operations and the changes in its financial position for the years then ended in accordance with generally accepted accounting principles applied on a consistent basis.

Calgary, Alberta
February 3, 1978

THORNE RIDDELL & CO.
Chartered Accountants

Notes to 1977 and 1976 Consolidated Financial Statements

NOTE 1 ACCOUNTING POLICIES

Principles of Consolidation

The consolidated financial statements include the accounts of the company and its wholly-owned subsidiary, Prairie Oil Exploration Ltd. to the date of its dissolution on November 25, 1977.

Depletion

The company follows the "full-cost method" of accounting whereby all costs related to the exploration for and the development of oil and gas reserves are capitalized, and depleted on a composite unit of production method based on total estimated recoverable reserves.

Depreciation

Depreciation of plant and equipment is being provided at rates which will amortize original costs over the estimated useful lives of the respective assets.

Income Taxes

The company follows the tax allocation method of accounting under which income tax provision is based on the earnings reported in its accounts. Under this method the company provides for deferred income taxes to the extent that income taxes otherwise payable are eliminated by claiming exploration and development costs and capital cost allowances in excess of the related depletion and depreciation provisions reflected in its accounts.

NOTE 2 PROPERTY, PLANT AND EQUIPMENT

	Cost	Accumulated Depletion and Depreciation	Net
December 31, 1977			
Oil and gas properties	\$11,327,849	\$2,977,756	\$ 8,350,093
Oil and gas production equipment	2,351,325	622,130	1,729,195
	<u>\$13,679,174</u>	<u>\$3,599,886</u>	<u>\$10,079,288</u>
December 31, 1976			
Oil and gas properties	\$ 9,229,062	\$2,613,369	\$ 6,615,693
Oil and gas production equipment	1,290,728	547,579	743,149
	<u>\$10,519,790</u>	<u>\$3,160,948</u>	<u>\$ 7,358,842</u>

NOTE 3 DIVIDEND RESTRICTION

The company is subject to the Anti-Inflation Act which provides for the restraint of dividends in Canada. Under the legislation, the company is restricted in the payment of dividends during the twelve month period ending October 13, 1978 to a maximum amount of \$1,385,000 based on its 1976 earnings.

NOTE 4 DIRECTORS' FEES

1977 general and administrative expenses include directors' fees of \$8,100.

PRAIRIE OIL ROYALTIES COMPANY, LTD.

COMPARATIVE SUMMARY

FOR THE YEARS ENDED December 31

	1977	1976	1975	1974	1973
Revenue (\$000)					
Oil Sales	\$ 378	\$ 312	\$ 253	\$ 194	\$ 173
Gas Sales	1,370	1,050	852	415	349
Royalties	983	688	477	665	654
Interest & Other	710	446	152	152	84
	<u>3,441</u>	<u>2,496</u>	<u>1,734</u>	<u>1,426</u>	<u>1,260</u>
Expenses (\$000)					
Production	\$ 321	\$ 201	\$ 163	\$ 160	\$ 144
General and administrative	188	135	108	97	51
Depletion	364	294	316	354	284
Depreciation	75	39	23	50	63
	<u>948</u>	<u>669</u>	<u>610</u>	<u>661</u>	<u>542</u>
Earnings before Income Taxes (\$000)	\$2,493	\$1,827	\$1,124	\$ 765	\$ 718
Income Taxes (\$000) (note 1)					
Current	232	147	(6)	(44)	—
Deferred	509	434	325	295	286
	<u>741</u>	<u>581</u>	<u>319</u>	<u>251</u>	<u>286</u>
Earnings before extraordinary item	1752	1,246	805	514	432
Extraordinary item	—	4,294	—	—	—
*Net Earnings (\$000)	<u>\$ 1752</u>	<u>\$5,540</u>	<u>\$ 805</u>	<u>\$ 514</u>	<u>\$ 432</u>
Net Earnings Per Share					
Before extraordinary item	89¢	63¢	41¢	26¢	22¢
After extraordinary item	89¢	\$2.82	41¢	26¢	22¢
Cash Flow before extraordinary item					
(\$000)	\$2,700	\$2,013	\$1,469	\$1,213	\$1,065
Per share	\$ 1.38	\$ 1.03	75¢	62¢	54¢
Expenditures (\$000)					
Exploration and property acquisitions	\$2,099	\$1,282	\$ 897	\$1,095	\$ 570
Plant and equipment (net after sales)	\$1,061	\$ 477	\$ 136	\$ 48	\$ (39)
Shares issued and outstanding	1,961,520	1,961,520	1,961,520	1,961,520	1,961,520
Market Price Ranges of Shares (\$)	High Low	High Low	High Low	High Low	High Low
American Stock Exchange 1st Quarter	11½ 8⅞	6 3½	4¾ 2⅞	11¾ 6¾	13⅞ 9
2nd Quarter	10⅞ 8¼	8¼ 4¾	5½ 3⅞	7⅞ 4⅞	9⅞ 6⅞
3rd Quarter	14⅞ 8	7¾ 6⅞	4⅞ 3¼	5⅞ 3	8¾ 6¼
4th Quarter	20⅞ 13½	11⅞ 6⅞	4 3	5⅞ 2¼	11¾ 5⅞

*Effective January 1, 1974 the Company adopted the deferred income tax method of accounting and 1973 earnings have been restated.

